July 15, 2003

Grain Inspection, Packers and Stockyards Administration
United States Department of Agriculture
Livestock and Meat Marketing Study
Room 1647-S
1400 Independence Avenue, SW
Washington, D.C. 20250-3604

Re: Livestock and Meat Marketing Study, Notice and request for comments (68 FR 32455).

Dear Sir or Madam:

This letter responds to Grain Inspection, Packers and Stockyards Administration's (GIPSA or the Agency) May 30, 2003, notice and request for public comment included in the Agency's notice pertaining to the development of a broad study of marketing methods used in the livestock and red meat industries as mandated by Congress.

The American Meat Institute (AMI) is the nation's oldest and largest trade association representing packers and processors of beef, pork, lamb, veal, and turkey, and processed meat products. Our member companies account for me than 90 percent of U.S. output of these products. AMI is supportive of efforts to comprehensively review the many board components that impact the marketing of meat and meat products from the farm to the table.

General Comments

During consideration of the Fiscal Year 2003 Agriculture Appropriations bill, H.R. 5263, the House Appropriations Committee specified the $4.5 million that the USDA/GIPSA is to use to conduct this study. The full House Appropriations Committee included accompanying report language to provide additional direction and clear intent for the use of these funds. Further, during consideration of the Omnibus Appropriations Act for Fiscal Year 2003 (Pub. L. 108-7), H.R. 5263 was incorporated into that measure, including the funding for this study. The following statement is the full excerpt that relates to the use of those funds for the study (House Rpt. 107-623):

> "*Packer Ownership.*--The Committee is very concerned about the economic impacts of Meat Packer Control, Feeding or Ownership of Livestock, and other captive supply issues, on local communities. The potential for shifts in livestock production, and the related shifts in live grain markets, for example, can impact local tax bases, as well as livestock and grain prices under Packer Ownership of Livestock. These types of swings can be significant to communities, and to independent producer viability.
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> The Committee is persuaded that the time has come for an earnest and objective study of the market and economic implications of laws that would prohibit meat packers from owning, feeding or substantially controlling livestock. The study should utilize expertise beyond traditional agricultural economics, including, but not limited to, industrial organization expertise and business school or business consulting expertise.
>
> Accordingly, the Committee directs the Secretary to conduct a study of the issues surrounding a ban on Packer Ownership, particularly as to the economic impacts on the United States as a whole, and on individual states. The study shall include, but not be limited to, examination of alternative procurement and transfer methods for livestock in the farm to retail chain, including producers that participate with packers in vertically-integrated livestock or meat production; agricultural credit for livestock producers; livestock and grain prices and the quality and consistency of meat products and livestock under a ban. The Committee provides a total of $4,500,000, to remain available until expended, for this study. The Secretary shall report the findings of the study to the House and Senate Committees on Appropriations within twenty-four months of enactment of this Act."

<u>Expertise Considerations</u>

Significant in the House Report language is the statement that "The study should utilize expertise beyond traditional agricultural economics, including, but not limited to, industrial organization expertise and business school or business consulting expertise." A number of the studies that have been conducted during the last 10 years examined the issues of packer ownership, livestock marketing, and related topics. However, those studies have been limited to more traditional agricultural economics fields and conducted predominately by agricultural university programs. For this study, USDA should approach non-traditional agricultural universities to seek out multi-disciplinary expertise in the business and marketing fields.

Much of the phenomena occurring during the last 20 years in marketing of animal protein products are a result of a more demanding ultimate customer base and an increasingly competitive marketplace for the food dollars of consumers. Universities, business school research programs, and institutions that have an expertise in examining the competitive pressures marketing issues placed upon industries and businesses can be of great benefit to fulfilling the intent of Congress in this study.

If this study is to provide useful, relevant material to the body of knowledge in this area, USDA will need to look beyond the results and scopes of previous studies of this subject matter. Livestock marketing is only a piece of the farm to table food chain. USDA should seek out institutions that can examine food marketing, financial analysis of producers and processors, capital and credit implications, risk and volatility management, operational design, organizational behavior, labor implications, vertical integration, dietary changes implications, the impact of state regulation, and related business fields.

Many leading U.S. universities that operate graduate level business programs provide excellent research services and skills in examining multi-discipline business and industry issues. USDA should contact these institutions to examine their interest in pursuing this study. Of the top 40 business school programs in the U.S. as ranked by Businessweek Magazine, 28 provide research programs and many have experience as government contractors for research services.

Scope, Parts, and Objectives

USDA's division of components of this study into parts and objectives is overly limited to a small segment of the value adding process and egregiously excludes major considerations in the marketing of meat and meat products, which directly relate to the procurements of livestock and inputs. USDA wrongly excluded economic drivers of the ultimate consumer, retailers, food service customers, institutions, and international customers from this study. Without adequate consideration for the ultimate consumers and the various segments of the farm to consumer marketing chain, USDA's study could exclude some of the most critical elements of market phenomena in the marketing of meat, meat products, and livestock.

Further, USDA over weighted issues concerning the "cash" or "spot" livestock market in its information collection and analysis parts and objectives. The parts and objectives also fail to examine questions of price volatility management, price risk, and the benefits and drawbacks to all parties of marketing and contracting agreements.

To correct these parts and objectives, USDA should consider the following modifications or suggestions. Parts 1 and 2, and the corresponding objectives 1 through 4, can be modified by adding the identification and survey of market drivers and economic demand considerations from the customer base of the packing community, including but not limited to, retailers, food service, institutions, government procurement, and international customers. Doing this would allow the study to examine the market drivers and implications and the marketing signals that have lead to an increasing use of marketing agreements among the meat and meat products marketing chain. Many marketing improvements in animal protein product offerings have occurred through the refinement of traits such as leaner products, convenience, tenderness, preparation ease, visual appeal, shelf life, food safety, texture, color, portion controlled, as well as price competitiveness. These are only a few of the many demand-based components that the USDA should consider when preparing its study. These traits are important to the producer processor relationship, because some of them require producer level management decisions to be brought to fruition.

Parts 4 and 5, and corresponding objectives 7 through 10, can be modified to examine the benefits and drawbacks of marketing agreements, including but not limited to, price risk management, price risk exposure, the benefits and drawbacks of marketing agreements for producers and processors, capital and credit implications of marketing agreements for producers and processors, capital and credit implications of for producers and processors that operate with limited or no marketing agreements, and related comparative studies among market participants.

Additionally, USDA should consider as an objective examination of the marketing relationships among all animal proteins and the role marketing agreements play in increasing or decreasing the competitive pressures and marketability of various animal protein products to the ultimate consumer. The *Federal Register* notice exclusively discusses cattle, hogs, and lamb, but excludes other animal proteins, including the nearly 40 billion pounds of poultry products that beef, pork, and lamb compete with in the marketplace annually. Without considering the competitive pressures all animal proteins place upon each livestock segment, USDA's study would be incomplete and fail to examine many of the largest marketing pressures on the industry.

Peer Review Considerations

The *Federal Register* notice includes USDA's intention to establish a five-to-seven member academic peer review group. USDA should consider using a similarly broad scope for assembling the peer review panel as provided in the House Report language for this study. "The study should utilize expertise beyond traditional agricultural economics, including, but not limited to, industrial organization expertise and business school or business consulting expertise," (House Rpt. 107-623). This process will allow for continuity throughout the study and ensure accountability for a multi-discipline study.

Appropriate Time Considerations

The House Report language provides that "The Secretary shall report the findings of the study to the House and Senate Committees on Appropriations within twenty-four months of enactment of this Act." This language would require the Secretary to complete and release the report findings sometime between now and February 20, 2005. However, recognizing the challenges of a study this broad and involved, USDA may want to consider seeking additional time to complete the study. Additional time would also provide for better times-series analysis and for a closer, more involved examination of the issues of this study.

Additional Considerations

The issues involved with livestock, meat, and meat products marketing have been on the forefront of Congressional debate for many years. Considerations of policies that prohibit livestock ownership, limit various forms of contracting and marketing agreements, spot market regulation, oversee contractual relationships, or impose marketing limitations within the meat industry have been debated in Congress and state capitols for many years.

More than 80 years ago, Congress acted on and passed initiatives to increase the regulatory scrutiny in this area and provide for the orderly marketing of livestock with its own statute. The Packers and Stockyards Act of 1921 is a statute unique to the meat industry that prohibits meat packers from engaging in unfair, deceptive, or fraudulent business practices that disadvantage their livestock suppliers. Additionally, the Sherman Act, the Clayton Act, the Robinson-Patman Act, the Agricultural Marketing Act, and the Uniform Commercial Code govern and regulate AMI's member companies' business practices nationally. To our knowledge, there is no other sector of the U.S. manufacturing or service economy in which the federal government plays such a watchdog role with respect to material suppliers. In short, the most appropriate government role in today's livestock marketing system is to enforce the existing laws and regulations that ensure fair and nondiscriminatory business practices among producers and packers, while allowing producers the freedom of choice on how best to market their livestock.

Two weeks ago, on June 21, 2003, the House Agriculture Committee's Subcommittee on Livestock and Horticulture held a field hearing in Grand Island, Nebraska on banning packer ownership. As the USDA prepares its request for proposals (RFP) for this study, it may want to examine the attached testimony from this hearing to understand some of the perspective as to the relevance and important role contracting and marketing agreements play in the meat and meat products marketing chain. The attached testimony is from J. Patrick Boyle, President and CEO of AMI.

Summary of Main Points

USDA should approach non-traditional agricultural universities to seek out multi-discipline expertise in the business and marketing fields. The USDA should seek out institutions that can examine food marketing, financial analysis of producers and processors, capital and credit implications, risk and volatility management, operational design, organizational behavior, labor implications, vertical integration, dietary changes implications, the impact of state regulation, and related business fields.

USDA should modify parts 1 and 2, and the corresponding objectives 1 through 4 by adding the identification and survey of market drivers and economic demand from the customer based of the packing community, including but not limited to, retailers, food service, institutions, government procurement, and international customers

USDA should modify parts 4 and 5, and corresponding objectives 7 through 10 to examine the benefits and drawbacks of marketing agreements, including, but not limited to, price risk management, price risk exposure, the benefits and drawbacks of marketing agreements for producers and processors, capital and credit implications of marketing agreements for producers and processors, capital and credit implications of for producers and processors that operate with limited or no marketing agreements, and related comparative studies among market participants.

USDA should examine the marketing relationships among all animal proteins and the role marketing agreements play in increasing or decreasing the competitive pressures and marketability of various animal protein products.

USDA should use a similarly broad scope for assembling the peer review panel as provided in the House Report language for this study.

Again, we appreciate the opportunity to provide input on this very important topic. We stand by to provide any additional information that may be critical in assisting the Agency in the development of this study.

Best wishes,

J. Patrick Boyle

Testimony of J. Patrick Boyle
President & CEO, American Meat Institute
Before the
House Agriculture Subcommittee on
Livestock and Horticulture

June 21, 2003

Thank you, Chairman Hayes, for inviting the American Meat Institute to testify here today.

AMI represents the interests of packers and processors of beef, pork, lamb, veal and turkey products and their suppliers throughout North America. Together, AMI's members produce 95 percent of the beef, pork, lamb and veal products and 70 percent of the turkey products in the U.S.

AMI's member companies' business practices are governed nationally not only by the Sherman Act, the Clayton Act, the Robinson-Patman Act and the Uniform Commercial Code, but also by the Packers and Stockyards Act, a statute unique to our industry that clearly prohibits meat packers from engaging in unfair or deceptive business practices that disadvantage their livestock suppliers. To my knowledge, there is no other sector of the U.S. manufacturing or service economy in which the federal government plays such a watchdog role with respect to material suppliers.

And yet, ironically, as the meat and poultry industry operates with this additional, daily, government oversight of our business transactions with livestock producers, we are here today to discuss whether meat packers should receive additional scrutiny, enforcement or business restrictions in order to protect or benefit livestock producers.

Questions about the structure of the meat industry have been raised throughout AMI's 100-year existence. While some suggest our laws and enforcement of them are inadequate, I would suggest another theory: perhaps we haven't done a good job of pinpointing some of the real problems and coming up with constructive solutions that benefit everyone.

Let me try to characterize the environment in which my member companies operate today. AMI members include 250 of the nation's largest and smallest meat and poultry food manufacturers. Collectively, they produce 95 percent of the beef, pork, veal and lamb food products and 70 percent of the turkey food products in the U.S.

AMI's members have one common objective: to produce products consumers will buy. It is the consumer who determines the value of our products, which in turn determines the value of our raw materials. So we must start any discussion with the consumer. Market research tells us that U.S. consumers have diverse tastes and that 95 percent of them eat meat and poultry regularly, so there is room in the marketplace for many different meat and poultry products with many different attributes. We also know that there is a robust global appetite for U.S. meat and poultry products. We now export 9.3 percent of our beef products and 6.9 percent of our pork products, principally to Japan, Mexico and Canada. These exports have grown exponentially in the past decade, in large part because we produce what consumers abroad want to buy.

In fact, livestock producers have raised and spent hundreds of millions of dollars over the past decade through check off programs designed to build consumer demand for beef and pork. A large part of these efforts has been to send clear signals from the consuming public back to producers, so that producers can deliver the type of livestock that will yield the meat products most in demand. These efforts have had many benefits, including improved communications throughout the meat chain among retailers, packers and producers. This, too, has led to vertical integration.

In order to create the foods people want to buy, AMI's members have done many things. They have increased their coordination with livestock producers so that the raw materials they purchase produce the foods consumers want to buy. They have increased their coordination with their retail and foodservice customers, sometimes changing management or operations in order to meet their customers' needs. This increased coordination has led to increased vertical integration, which has sometimes included complete or partial ownership of some of each packer's livestock supply. Some positive outcomes of this increased coordination may be familiar to you:

Leaner Beef and Pork for Consumers. Retailers, meat packers and livestock producers heard loud and clear in the 1980s that consumers wanted leaner meats. Working together, these three sectors accomplished an average 27 percent fat reduction in a serving of beef and a 31 percent fat reduction in a serving of pork. Among the actions taken were: packers and retailers trimming fresh meats to ¼-inch of external fat; hog producers and pork packers working together to develop leaner hogs; cattlemen and meat packers petitioning USDA to create a new "Select" grade for leaner beef; and meat processors developing vast new offerings of low-fat hot dogs, luncheon meats, ham, sausage and bacon products. Increased coordination among producers and packers has provided for greater information exchange, helped improve herd management, and aided producers to deliver at the optimum time, which are all essential items that have assisted in producing a leaner, more desirable products.

Improved Risk Management Options for Producers. The volatility inherent to farming and ranching has been reduced for many livestock producers through the increased use of contracted sales with meat packers and many other creative risk management plans. The benefits to farmers were perhaps most vivid during the hog market crash of 1998, when spot market prices for an unanticipated over-supply of hogs dropped to as low as $9 per cwt. Those hog farmers with contracts had locked into much higher prices for their hogs – generally $35 and more per cwt. – and were protected from the low market prices. Packers with contracts, on the other hand, were obviously paying far over the market value for their hogs at the time. Both parties to the contract, however, benefited from the certainty provided by a steady, consistently priced, contracted supply of hogs.

More Options for Young Producers. During the past three decades, the average age of livestock producers has been steadily increasing. This is of great concern to the packing community who are dependent on reliable supplies of quality inputs at affordable prices. Contracting options, marketing agreements, and other producer-packer arrangements provide a means for young producers to access the capital necessary to carrying on or enter the livestock production profession. Many young people have the educational background and herd management knowledge but lack the ability to enter because of the capital requirements. Arrangements between producers and packers assist in retaining the valuable herd management knowledge in the production agriculture segment of our economy.

Steady Investment for Rural America. A majority of AMI's 250 members operate their plants and facilities in towns with populations under 100,000. The economic value and employment generated from our member's operations are significant economic drivers in hundreds of rural and mid size communities across America. An essential component to their ability to continue to employ thousands of individuals in their facilities is the assurance of a reliable supply of inputs. Contractual relationships, marketing agreements, and other arrangements provide a means to ensure that the facilities can run at optimum levels and can make planning decisions for their daily, weekly, and monthly operations. Ill conceived limitations on the procurement process place into jeopardy the ability for plants to reasonably anticipate workforce requirements on a daily, weekly, and monthly basis. Producer-processors arrangements provide a means for processors to adequately plan workforce needs.

Before I leave this topic of the benefits of coordination and even integration between manufacturers and their suppliers in the meat industry, I would just note that this is a trend throughout the manufacturing and service economy. It is driven largely by consumer demand for consistent product quality at the lowest possible price. The demand for low prices has led to fewer and larger retail chains in fields as diverse as home improvement products (Home Depot), video rentals (Blockbuster), food and consumer products (Wal-Mart) and fast food (McDonalds). In fact, these companies not only owe their success to these qualities and business practices, they advertise them to consumers. The consolidation at the retail level has driven consolidation at the manufacturer level – for tools, appliances, consumer goods and food products, among others. The demand for consistent product quality has led many firms to exert greater control over their supply chain. Just ask anyone who supplies products to Wal-Mart or McDonalds what that means: it means you must meet their standards or you can't sell to them. It often means you must subject your products and plants to periodic customer audits. This is the way business is done today – and the meat industry should be no exception.

Against this backdrop I have described of businesses trying to compete for the consumer's dollar, I hope you can understand why the American Meat Institute strongly opposes efforts that would make it illegal for meat manufacturers to do what the rest of the global business community is doing, which is to form relationships with suppliers of raw materials in order to produce consistent quality, low-priced products that consumers will buy. In our view, the proposed ban on packer ownership, control or feeding of livestock would do just that. Further, we will oppose any effort to restrict meat packers who comply with existing antitrust and fair business practice laws from sourcing their raw materials in any way. It is unfair to make it illegal for the meat industry to compete with the poultry industry or any other industry for the consumer's dollar. But let us not forget the ultimate consumer during this debate.

Over the last three decades, Americans have benefited from increasing meat industry efficiency that has made meat more affordable, abundant, convenient and varied. Each year, consumers spend less of their disposable income on meat and poultry. Today, that number stands at 1.9 percent, compared to 4.1 percent in 1970. This is a trend of which we are proud – and one that provides consumers a distinct benefit. We should not rush to undo the foundations of this success without understanding the ramifications for everyone involved.

AMI has long standing policy in opposition to legislation proposing to ban packer ownership, feeding or control of livestock. We believe the strength of the current livestock marketing system in the U.S. is the flexibility it provides to producers, packers/processors and retailers in responding to market signals, while maintaining a variety of choices for the producer through to the consumer. Producers have a multitude of options in marketing their livestock: spot market transactions, cooperatives, bargaining associations and other programs that allow them to align themselves with packers through contractual arrangements to manage risk.

We believe that the most appropriate government role in today's livestock marketing system is to enforce the existing laws and regulations that ensure fair and nondiscriminatory business practices among producers and packers, while allowing producers the freedom of choice on how best to market their livestock. The government should exercise its current and vast authority under the Sherman Act, the Clayton Act, the Robinson-Patman Act, the Packers and Stockyards Act and other state codes.

If there is consensus that the livestock market is not working properly, then we advocate a thoughtful, reasoned, fact-based approach that will help all businesses – farms, ranches, processors and retailers -- pinpoint problems and develop targeted and effective solutions.

In fact, as you continue to contemplate possible policy changes to the current marketing system for livestock, we would like to remind you of an important provision included in the Omnibus Appropriations Bill for FY 2003, which provides $4.5 million to USDA to conduct a comprehensive study on this subject. The provision requires the Secretary of Agriculture to conduct a study of the issues surrounding a ban on packer ownership, particularly as to the economic impacts on the United States as a whole, and on individual states. The study shall include, but not be limited to, examination of alternative procurement and transfer methods for livestock in the farm to retail chain, including producers that participate with packers in vertically-integrated livestock or meat production; agricultural credit for livestock producers; livestock and grain prices and the quality and consistency of meat products and livestock under such a ban.

On May 30, 2003, GIPSA released a notice seeking comment on the parameters of the study. There will we a formal Request for Proposals for the study itself after USDA reviews the comments from this notice. The comment period closes on June 30.

Again, thank you for the opportunity to testify before your committee on this important issue.

Attachment: J. Patrick Boyle's Statement before the House Agriculture Committee's Subcommittee on Livestock and Horticulture's June 21, 2003 field hearing.